

**THE PROTECTION OF MINORITY SHAREHOLDERS IN SOUTH AFRICA:
A REFLECTION ON THE DERIVATIVE ACTION, APPRAISAL RIGHTS
AND OPPRESSION REMEDY**

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Chapter 1: A prelude to the discussion on minority shareholders' rights

1.1 A background to company law and majority rule

The wheel of corporate law turns on the principle of majority rule, a rule that was established in the case of *Foss v Harbottle*.¹ The decision-making process of a company is based on the rule of majority votes, which means that shareholders who own fifty percent or more of the voting shares carry the vote.² The majority rule system poses great advantages as it allows persons with a greater investment in a company to determine the decisions pertaining to the management of the company. The majority rule principle ensures an efficient operating mechanism for companies by removing the prospect of a few minority shareholders vetoing decisions of the majority. Persons that become shareholders in a company do so with the understanding that they will be legally bound by the decisions of the majority shareholders³ as it pertains to matters of corporate governance.⁴

However, if unchecked, the majority shareholders may abuse their voting powers to the detriment of minority shareholders. For example, the majority can vote for a resolution that is of no financial benefit to the company or the majority shareholders can ratify the wrongful actions of company directors. For this reason, there is a need for effective minority shareholder protective measures to guard against the abuse of the powers wielded by the majority shareholders. The protection of minority shareholders is not only essential for the benefit of individual minority shareholders or ensuring equality in the corporate sector, but also for its contribution towards the growth of economies, particularly in developing countries with emerging economies.⁵

There is a direct link between effective minority shareholder protection and economic growth.⁶ A country that has effective protective mechanisms to guard against the abuse mentioned above

¹ *Foss v Harbottle* 1843 (2) Hare 461, 67 ER 189.

² *Louw and Others v Nel* 2011 (2) All SA 172 at 30, stating that the *Foss v Harbottle* has two rules that is, the principle of majority rule, that a company's affairs are determined by the majority of votes in the company and that the company must assert its rights itself (the proper plaintiff rule).

³ Shareholder(s) that own more than fifty percent of the shares of the company. This could be one shareholder owning more than fifty percent or the majority ownership could be divided amongst more than one shareholder.

⁴ *Sammel v President Brand Gold Mining Co Ltd* 1969 (3) SA 629 (A) at 678. Note that corporate governance is broadly defined as a code of conduct and set of principles by which companies must be directed and controlled. Dennis Davis & Davis Walter (eds) *Companies and Other Business Structures in South Africa* 3 ed (2013) 447.

⁵ Mauro F Guillen & Laurence Capron 'State Capacity, Minority Shareholder Protections, and Stock Market development' (2016) 61 (1) *Cornell University Administrative Science Quarterly* 25-160 at 128.

⁶ Mauro F Guillen & Laurence Capron 'State Capacity, Minority Shareholder Protections, and Stock Market development' (2016) 61 (1) *Cornell University Administrative Science Quarterly* 125-160 at 133.

is more likely to attract foreign investors than a country without minority shareholder remedies. Financiers are more inclined to invest in markets with effective and adequate protection policies for the minority shareholders as this provides an indication of the safety of their investments.⁷ Furthermore, establishing effective minority protection encourages dispersed share ownership within a market which is argued to be beneficial to the development of the stock market and overall economic growth.⁸ It follows therefore that for any developing country, the protection of minority shareholders should be chief amongst its company law reform objectives. The Companies Act 71 of 2008 (hereafter referred to as the Companies Act) ushered in improved remedies for the protection of minority shareholders' rights.⁹ This thesis will interrogate the redress mechanisms in South African legislation and their effectiveness in assisting minority shareholders to obtain relief when their rights and interests have been infringed.

Although it has been established that the majority rule prevails and that minority shareholders knowingly agree to be bound by the decisions of the majority, it does not follow that minority shareholders are without any rights.¹⁰ The need for an analysis of the protection afforded to minority shareholders is based on the understanding that whilst there are sufficient principles and doctrines protecting the rights of majority shareholders and the company, the same cannot be said for minority shareholders.¹¹ For example, principles such as the majority rule alluded to earlier, the business judgment rule¹² and the principle of separate legal personality¹³ all work to enshrine the interests of the majority shareholders. Whilst these doctrines are very crucial to the independence and well-functioning of the company, there must be legal provisions to guard against possible abuse. It has been argued that the majority rule, when unchecked, can

⁷ Guillen supra, note 6 at 133.

⁸ Guillen, supra note 6 at 125-160 at 127-8.

⁹ This is in specific reference to the derivative action, the oppression remedy and the introduction of the appraisal rights. These remedies will be discussed in detail in later chapters.

¹⁰ Each company's Memorandum of Incorporation lays out the rights and duties of the shareholders. Furthermore, the Companies Act provides relief that is specific to minority shareholders. The following sections will provide a full discussion on the said reliefs.

¹¹ This is evidence by the fact that minority shareholder rights are the exception to the rule and not the rule itself. The courts' starting point is usually upholding the corporate principles of majority rule and the business judgment rule.

¹² The business judgment rule is a common law principle which has been codified under section 76 (4) of the Companies Act. It means that a director is not in breach of his duties if he or she had taken reasonably diligent steps to inform him/herself of the matter in question and had a rational basis for believing that his or her decision was in the best interests of the company.

¹³ This is a common law principle that establishes the juristic personality of a corporation and its independence from its shareholders. There are legal consequences flowing from this which will be discussed in chapter two.

encourage or aid acts of self-dealing and or oppressive acts.¹⁴ The situation created is an imbalance in the protection of rights afforded to the parties which balance is crucial to the functioning of the company. The continued abuse of corporate powers will culminate in stifled shareholders' activism, erosion of corporate governance principles and the loss of confidence by investors in the system.

The existence of robust shareholders' remedies can encourage shareholders to actively challenge the decisions of the board of directors and management. This in turn, encourages proper corporate governance practices.

South Africa has minority shareholder protection measures to guard against the abuses mentioned above. There are various legal measures contained within the Companies Act. This thesis will focus on three particular remedies, namely, the derivative action, appraisal rights, and the oppression remedy.

1.2 Aims of the thesis

The aim of this research is to determine whether minority shareholders are adequately protected under the Companies Act in South Africa. To that effect, this paper will consist of a discussion of the three main minority protection provisions, each provision will be critiqued separately in order to judge the practical effectiveness.

South Africa is not the only African country that has embarked on the journey to reform its company laws, specifically provisions protecting minority shareholders. Other developing countries have prioritised the improvement of minority shareholder protection. Zimbabwe has for the past several years been working on reforms to its Companies Act.¹⁵ The paper will also consist of a comparison of the South African company law to the new Companies and Other Business Entities Act of Zimbabwe.¹⁶

1.3 Research questions

This research will attempt to answer the following question:

¹⁴ Peter J. Horne, 'Suppressing minority Shareholder Oppression' (2013)16.2 *Duquesne Business law Journal* at 205.

¹⁵ As evidence by the Zimbabwean Companies and Other Business Entities Act, 2018.

¹⁶ Companies and Other Business Entities Act, 2018.

How can the legislative provisions, providing for the protection of minority shareholders be improved or supplemented in a way that ensures the availability of effective and practical redress measures for minority shareholders?

1.4 Significance of the thesis

The introduction has highlighted that the laws on the protection of minority shareholders have a direct impact on the economic growth and should, therefore, be prioritised. The significance of this thesis is to provide a critique of three specific minority protection provisions in the Companies Act and highlight the shortfalls of these remedies. Following that, this thesis will recommend amendments to the legislation that will contribute towards achieving reasonable levels of practicality and effectiveness in the implementation of those remedies. Finally, this thesis will also highlight the role of the courts in achieving the balance between majority and minority shareholders.

1.5 Methodology

This thesis will be conducted by reviewing South African literature that is published in various primary and secondary sources. The research will refer to key South African statutes namely, the South African Companies Act, the Constitution of the Republic of South Africa, 1996 (hereafter referred to as the Constitution) and the Promotion of Access to Information Act 2 of 2000. Parallel statutes of Zimbabwe, Canada, and the United States of America will also be referenced throughout this thesis.

Additionally, this thesis will review case law relating to the subject and the *ratio* of those cases will be analysed. The role of the courts in interpreting certain legal provisions will be important in assessing whether the courts have adopted a liberal or restrictive approach to the issue of protecting minority shareholders.

A comparative analysis will be conducted to evaluate how South African company law has dealt with the issue of the protection of minority shareholders. This thesis will therefore compare and contrast South African and Zimbabwean legislation and case law on minority shareholder remedies. This will be achieved by evaluating how the two nations implement and apply legislation providing for the protection of minority shareholders. As part of this analysis, this thesis will review what Zimbabwe can learn from the South African system

1.6 Chapter outline

Chapter two will discuss the derivative action as outlined in section 165 of the Companies Act. This chapter will provide a brief history of the foundations of the derivative action and its evolution. This background will serve as a point of departure for further discussion relating to the class of persons who can use the remedy, the procedures, the various tests outlined, the available relief and the burden of costs. Chapter two will also provide a discussion of the case law pertaining to the derivative action. Finally, chapter two will compare and contrast the derivative action in Zimbabwe to South Africa.

Chapter three will review the appraisal rights provided for under section 164 of the Companies Act. This chapter will focus on the purpose of appraisal rights to minority shareholders and the companies' outlook on the effect of appraisal rights. More importantly, chapter three will focus on the procedural aspects of asserting appraisal rights and their impact on minority shareholders and companies involved. Finally, chapter three will compare appraisal rights in Zimbabwe to South Africa.

Chapter four will be a discussion of the oppression remedy as provided for under section 163 of the Companies Act. This section will discuss the various situations that justify the application of the oppression remedy. There is a list of legal requirements that the shareholder must satisfy before the court can grant them relief. Therefore, this thesis will investigate the reasonableness of satisfying those legal requirements. The courts' approach in interpreting this remedy and the responsibilities of the shareholders will also be examined. Furthermore, this thesis will deal with the definitions of various concepts that form the core of this remedy. Chapter four will also deal with the procedural requirements and relief orders from which the courts can choose and their suitability to affected minorities. Finally, chapter four will compare the Zimbabwean application of the remedy to South Africa.

Chapter five will conclude with a summary of the findings on the three remedies with respect to South Africa and Zimbabwe. Following the summary, there will be recommendations on steps and policies that the legislator, the beneficiaries of remedies and the respective nations of South Africa and Zimbabwe can implement to improve the effectiveness of the derivative action, appraisal rights and oppression remedy.

Chapter 2: A discussion of the derivative action in South Africa

2.1 An introduction to the South African derivative action

South African company law recognises the principle of separate legal personality as established in the case of *Salomon v Salomon*.¹⁷ This principle acknowledges that a company is a juristic person distinct from its shareholders and directors.¹⁸ Furthermore, the company can sue and be sued for its rights and obligations respectively in its own name, through the persons managing it.¹⁹ In the case of *Foss v Harbottle*, the court established the proper plaintiff principle which means that in an action in respect of a wrong alleged against the company, the proper plaintiff is *prima facie* the company itself.²⁰ As explained in *Wallersteiner v Moir* the proper plaintiff rule in *Foss v Harbottle* is easy to enforce when the company is wronged by outsiders or by the minority.²¹ In such instances, the majority can simply call for a general meeting in terms of the Memorandum of Incorporation (MOI)²² of the company and resolve to institute legal action to enforce the company's rights. However, this is not the case when the wrongdoers are in control of the company or when they hold the majority vote.²³ In such instances, the directors, with the support of the majority shareholders may decline to commence litigation for the company for fear that their actions will be brought to light and they are reprimanded.²⁴

In the interests of justice, the courts will recognise a few exceptions to the rule in *Foss v Harbottle* and shareholders or other persons may be allowed to bring an action in their own name on behalf of the company against the wrongdoers.²⁵ The courts will allow this where it is clear that the wrongdoers are in control of the company, and through their power, will not allow any action to be brought in the name of the company.²⁶ Lord Denning justified the need for the exceptions stating that, ‘...in one way or another some means must be found for the company to sue. Otherwise, the law would fail in its purpose. Injustice would be done without

¹⁷ *Salomon v A Salomon & Co Ltd* 1896 UKHL1, 1897 AC at 22.

¹⁸ *JCI Letseng diamonds citing John Shaw and Sons (Silford Ltd v Shaw)* 1935 (2) KB 113 (CA) at 134.

¹⁹ Farouk HI Cassim (ed), Maleka Femida Cassim, Rehana Cassim *et al Contemporary Company Law* 2ed (2012) at 31 (hereafter *Contemporary Company Law*).

²⁰ *Foss v Harbottle* 1843 (2) Hare 461; 67 ER at 189 (hereafter *Foss v Harbottle*).

²¹ *Wallersteiner v Moir* (No.2) 1975 (1) ALL ER at 849 (CA) (hereafter *Wallersteiner v Moir*).

²²This is defined as a document that amounts to a constitution of the company, which sets out the rights, duties of shareholders and directors, the authorized share capital of the company and other matters. Companies and Other Business Structures glossary at 452.

²³ *Minister of Mines & Mining Development & Others v Grandwell Holdings (Pvt) Ltd & Others* SC 34/18|1.

²⁴ *Wallersteiner v Moir* (No2) [1975] 1 All ER 849 (CA) at 875 d-f.

²⁵ *L. Piras & Son (Pvt) Ltd & Another Intervening v Piras* 1993 (2) ZLR at 245 where the Chief Justice upheld the ruling of the lower court arguing that the derivative action is such an exception to the rule in *Foss v Harbottle*. The court allowed the defendant to intervene to protect the interests of the company.

²⁶ James Thomas Riley Gibson, Coenraad Visser *South African Mercantile & Company Law* 8 ed (2003) 370-371.

redress.²⁷ Allowing minority shareholders to bring a derivative action affords the company justice and the wrongdoers are held accountable. Therefore, the derivative action provides the answer in allowing persons other than the company to sue on behalf of the company. The derivative action can be described as a two-fold action. On one hand, it is the equivalent of a suit by the shareholders to compel the corporation to sue and on the other, it is a suit by the corporation, asserted by the shareholders on its behalf, against those liable to it.²⁸

The derivative action has gone through an evolution in South Africa. The evolution has seen a departure from the restrictive common law derivative action that offered little help to minority shareholders to a codified derivative action²⁹ that serves the interests of minority shareholders better.³⁰ Section 165 of the Companies Act begins with the abolition of the common law derivative action which had co-existed with section 266 of the old Companies Act 61 of 1973.³¹ Any derivative action brought before the courts must be done within the parameters of section 165 of the Companies Act. The derivative action was expanded and improved specifically in terms of the cause of action, the identity of the wrongdoer and persons who have legal standing to institute legal proceedings on behalf of the company.³² The following sections will discuss these three areas in more depth.

As stated above, the derivative action is an exception to the general rule that shareholders cannot institute proceedings on behalf of the company. The derivative action must be distinguished from direct action, for example, an application for relief from oppressive conduct.³³ The latter is a direct application made by a shareholder in their personal capacity, for wrongs committed against them whereas the former is for wrongs committed against the company.³⁴ In essence, the derivative action affords persons with an interest in pursuing justice and obtaining redress for a company the channel to do so where the company declines to do so.³⁵

²⁷ *Wallersteiner v Moir* (No2) 1975 (1) ALL ER 849 (CA) at 857 f.

²⁸ *Aronson v Lewis* (Del. 1984) 473 A.2d at 805-811.

²⁹ The Memorandum on the Objects of the Companies Bill, Companies Bill [B 61D-2008] specifies that section 165 of the Companies Act codifies and streamlines the derivative action together with the elimination of the common law derivative action.

³⁰ Van Wyk de Vries Commission of Enquiry into the Companies Act, Mann Report RP 45/1970 at 42.10-18 stated that the common law- derivative action was stringently limited by the *Foss v Harbottle* rule, had such a narrow field as to be virtually insignificant, and was beset with procedural difficulties.

³¹ Companies Act, section 165 (1).

³² *Contemporary Company Law* at 777.

³³ The term oppressive conduct will be discussed in later chapter four.

³⁴ Companies Act 71 of 2008, section 165(2).

³⁵ *Lewis Group Limited v Woollam & Others* 2016 ZAWCHC 130 at 49.

Any person approaching the courts for relief must, in terms of the Companies Act, satisfy the stated legal requirements before the courts can grant relief.³⁶ The litigant must prove that they have legal standing and that the company has refused to file the lawsuit.³⁷ In addition, the litigant must establish the merits of their case by satisfying various tests.³⁸ This thesis will focus on the legal requirements and how they affect minority shareholders intending to enforce their rights and seek protection from the courts.

2.2 Discussing persons with legal standing under section 165

In terms of section 165 (2) of the Companies Act, the derivative action can be brought by the following classes of people: shareholders, directors or prescribed officers of the company or a related company, registered trade unions or other employee representatives and any persons granted leave by the courts to bring such a suit. This is a wide pool of persons which extends to more than just minority shareholders. This is a positive development, allowing other persons with the means to bring an action on behalf of the company the legal avenue to do so. The inclusion of trade unions increases the prospects of minority shareholders attaining relief, particularly for employees participating in employee ownership schemes³⁹ and therefore have interests to protect. Whilst shareholders might be able to condone a loss, it is the employees who might bear the loss in the form of wage and salary cuts. Therefore, such parties must be allowed to approach the courts where necessary.⁴⁰ The court also has the discretion to allow any other persons it deems fit to commence or continue litigation on behalf of the company.⁴¹ This is a recognition that persons other than shareholders also have a legitimate and cognisable interest in the assertion or defence of a company's legal interests.

2.3 The procedure under section 165 of the Companies Act

A litigant is required to serve a demand on the company to commence or continue legal action in order to act on behalf of the company before making an application to the court.⁴² This is to afford the company time to conduct its due process and apply its judgment on the merits of the

³⁶ Companies Act, section 165(12).

³⁷ Companies Act, section 165(2).

³⁸ Companies Act, section 165(5)(b).

³⁹ Defined as a scheme established by a company by either a means of a trust or otherwise for the purpose of offering participation to employees, by means of issue of shares in the company. Companies Act, section 95 (1) (c).

⁴⁰ *Lewis Group Limited v Woollam & Others* 2016 ZAWCHC 130 at 33.

⁴¹ Companies Act, section 165(2)(d).

⁴² Companies Act, section 165(2).

allegation.⁴³ Pursuant to receiving such a demand, the company has the option to first issue an outright refusal followed by an application to the court to dismiss the applicant's demand⁴⁴ and secondly the appointment of an independent person to investigate the demand and the surrounding circumstances and report to the board of directors.⁴⁵ This may also be followed by the company's decision to proceed with the suit

The Companies Act does not prescribe what the demand served on the company should contain. However, the courts argued that if a demand is to withstand a challenge from the directors, it must have a substantial claim in respect of the matter because the demand will be used as a framework for the independent investigation.⁴⁶ The demand must have cogency, albeit not with the precision required for pleadings but it must provide the basis for the company to institute or continue with litigation.⁴⁷ The demand on the company and the application for leave serve to provide a filter to sift meritless cases. Furthermore, the statutory provision requiring the independent investigator to report to the board of directors and not to the complainant ensures that the demand process is not used by litigants as a fishing expedition for facts to establish an action.⁴⁸

Although the appointment of an independent investigator should be applauded, the unilateral appointment of the expert poses questions of whether the investigator can be impartial. The investigator is appointed and remunerated by the company.⁴⁹ Leaving the selection of the investigator to one party leaves room for bias, for example, the company could choose an investigator that is sympathetic to the majority's agenda.⁵⁰ The Companies Act does not mention the extent of the cooperation required of the company during the investigation. It is submitted that the appointment of an impartial investigator must be done with the input of both the litigant and the company. If the company consulted the litigant during the appointment of the independent investigator it would eliminate any suspicion of bias, as was stated in the case of *R v Sussex Justice Ex parte McCarthy* 'not only must justice be done, it must also be seen to

⁴³ Companies Act, section 165(4). The company completes this process through the mandated hiring of an independent investigator who must assess the complaint and give recommendations on whether the company should commence litigation.

⁴⁴ Companies Act, section 165(3).

⁴⁵ Companies Act, section 165(4)(a).

⁴⁶ *Lewis Group Limited v Woollam & Others* (3) 2017 SA 15 at 56.

⁴⁷ *Lewis Group Limited v Woollam & Others* (3) 2017 SA 15 at 47.

⁴⁸ The scope of the investigation is limited to the particular claim and the facts surrounding it through section 165 (4) (a) (i).

⁴⁹ Companies Act, section 165(4)(a).

⁵⁰ *Lewis Group Limited v Woollam & Others* (3) 2017 SA 15 at 45.

be done.’⁵¹ Thus, allowing the input of the litigant in the selection process will to an extent validate the impartiality of the investigating officer and instil confidence of the litigant in the report.

2.4 A scrutiny of the legal requirements

2.4.1 The test for a show of good faith

To minimise the risk of flooding the courts with meritless derivative litigation, the legislature placed safeguards or requirements that each litigant must satisfy before the court can hear an application.⁵² Once the litigant has established their legal standing, they must satisfy the court that the application is made in good faith in accordance with section 165(5)(b)(i) of the Companies Act. The Companies Act does not, however, provide a definition for good faith. An illuminating discussion regarding the criterion of good faith has been offered.⁵³ It has been said that the doctrine of good faith is an elusive subject, whose interpretation can be understood from the meaning of common law principles together with the directors’ fiduciary duty to act in good faith and in the best interests of the company.⁵⁴

The court in *Mouritzen v Greystone* explained that a litigant that demonstrates ‘good conscience and sincere belief on the existence of reasonable prospects of success in the proposed litigation and, therefore, the absence of ulterior motive, on the part of an applicant’ would have demonstrated the good faith.⁵⁵ In *Swansson v Pratt*, it was explained that the court will consider whether the litigant believes that the case is based on a good cause of action which has a reasonable prospect of success. However, if the litigant is bringing the suit for a collateral purpose that would amount to an abuse of the process.⁵⁶

The first step in ascertaining good faith involves both a subjective and an objective test. The subjective test questions whether or not the litigant honestly believes that there is a valid cause of action whilst the objective test questions whether a reasonable man in the position of the

⁵¹ *R v Sussex Justice Ex parte McCarthy* KB EWHC at 256.

⁵² Maleka Femida Cassim *The statutory derivative action under the companies Act of 2008, Guidelines for the exercise of the judicial discretion*. (Unpublished PhD thesis, University of Cape Town, 2014) at 34.

⁵³ Maleka Femida Cassim ‘The statutory derivative action under the Companies Act of 2008: The role of good faith’ (2013) 130 (3) *SALJ* at 496-526.

⁵⁴ Maleka Femida Cassim *The statutory derivative action under the companies Act of 2008, Guidelines for the exercise of the judicial discretion*. (Unpublished PhD thesis, University of Cape Town, 2014) at 30.

⁵⁵ *Mouritzen v Greystone Enterprises (Pty) Ltd & Another* 2012 (5) S KZD at 103.

⁵⁶ *Swansson v Pratt* 2002 (42) ACSR 313.

litigant would believe that a valid cause of action exists.⁵⁷ However, it is a difficult task for the courts to measure a litigant's belief in their case. The courts simply will not accept a bold assertion, therefore the litigant must provide a cause for belief.⁵⁸ In *Mbethe v Manganese*, the courts emphasised the point that a mere assertion by the litigant will not suffice.⁵⁹ Qualifying that although the good faith test is in nature subjective as it relates to the mind of the litigant it must therefore, be subjected to an objective test.⁶⁰ The courts can only determine the state of mind of the litigant by drawing inferences from the objective facts as they appear from the evidence submitted by the litigant.⁶¹ In order to satisfy this test, the litigant would require evidence in the form of company records which the litigant might not have access to. Therefore, the company must allow sufficient access to the company records for minority shareholders to successfully prepare their case.

Nevertheless, in other jurisdictions, the courts have allowed actions to proceed based upon the information and the belief of others.⁶² The courts acknowledged that minority shareholders are invariably at a disadvantaged position preventing them from obtaining first-hand evidence and information upon which to base their application.⁶³ In interrogating the second aspect of the test, the litigant must satisfy the court that bringing the suit would not amount to an abuse of the process but is a necessary act in pursuit of the best interests of the company.⁶⁴

2.4.2 The test for the trial of a serious question

A litigant must satisfy the court that the derivative action is neither frivolous nor vexatious.⁶⁵ The litigant is required to show that there is a serious question to be tried that is of material consequence to the company.⁶⁶ In contrast with the *prima facie* test,⁶⁷ the threshold of proof

⁵⁷ Maleka F. Cassim The statutory derivative action under the companies Act of 2008, Guidelines for the exercise of the judicial discretion. (Unpublished PhD thesis, University of Cape Town, 2014) at 31.

⁵⁸ M A Maloney 'Whither the Statutory Derivative Action' (1986), 64 *Can. B. Rev* 309 at 326.

⁵⁹ *Mbethe v United Manganese (Pty) Limited* 2017 All SA at 67.

⁶⁰ *Mbethe v United Manganese (Pty) Limited* 2017 All SA at 67.

⁶¹ *Mbethe v United Manganese (Pty) Limited* 2017 All SA 67 at 20.

⁶² M.A. Maloney 'Whither the Statutory Derivative Action' (1986), 64 *Can. B. Rev* 309 at 326 citing *Armstrong v Gardner* (1970), 20 O.R. (2ed) 648 (Ont.H.C).

⁶³ M. A. Maloney 'Whither the Statutory Derivative Action' (1986), 64 *Can. B. Rev* 309 at 326 citing *Armstrong v Gardner* (1970), 20 O.R. (2ed) 648 (Ont.H.C.).

⁶⁴ Companies Act, section 165(5)(b)(iii).

⁶⁵ Maleka Femida Cassim The statutory derivative action under the companies Act of 2008, Guidelines for the exercise of the judicial discretion. (Unpublished PhD thesis, University of Cape Town, 2014) 62 .Dr. Maleka explains that section 165 gives power to the courts to act the gate keepers of the derivative action by discarding cases without merit thus weeding the good cases from the bad. The test on the trial of a serious question examines the merits of the case. Thus litigants must prove their case.

⁶⁶ Companies Act, section 165(5)(b)(ii).

⁶⁷ *Beecham Group Ltd v B-M Group (Pty) Ltd* 1977 (1) SA 50 (T).

for the trial of a serious question on the merits of the case is relaxed and lower.⁶⁸ Notably, authors have commended the legislature stating that, ‘the modern criterion of the trial of a serious question is in keeping with the policy principle that leave applications for derivative actions should be relatively simple short and inexpensive.’⁶⁹

The litigant must, in addition, prove that the question to be tried is of material consequence to the company.⁷⁰ Clearly, this is a safeguard against the pursuit of *bona fide* claims whose benefits will not justify the cost of instituting or defending such claims. The courts will uphold the presumption that the directors acted in the best interests of the company by not pursuing a claim whose benefits would be inconsequential to the company.⁷¹

2.4.3 The test for the best interests of the company

Finally, the litigant must satisfy the court that it would be in the best interests of the company to initiate the derivative claim.⁷² When the directors of a company refuse to commence or continue with the legal process, a rebuttable presumption arises that the directors’ decision against prosecuting the matter was made in the best interests of the company.⁷³

Companies are in the business of generating revenue, therefore, any time or resources that are diverted from that cause may, in my view, be considered as acts that are not in the best interests of the company.⁷⁴ The best interests of the company relate to business decisions that favour the interests of the current and future shareholders of the company.⁷⁵ The test for the best interest of the company looks at the commercial viability of the claim instead of the legal viability.⁷⁶

⁶⁸ Cassim supra, note 67 at 59 commends this change by the law makers stating the lower threshold eliminates the risk of the courts prematurely conducting a trial of the merits at the stage of application for leave to bring the case.

⁶⁹ Maleka Femida Cassim The statutory derivative action under the companies Act of 2008, Guidelines for the exercise of the judicial discretion. (Unpublished PhD thesis, University of Cape Town, 2014) 62.

⁷⁰ Cassim supra, note 62 at 57.

⁷¹ Section 165(7) read together with section 76 of the Act which codifies the business judgment rule. The justification for this presumption is aptly described by Davis *et al Companies and other Business Structures in South Africa* (2011) 16 stating that the Companies Act as a whole tries to limit over-regulation by ensuring that it is the board of directors who run the companies and not regulators and judges.

⁷² Companies Act, section 165(5)(b)(iii).

⁷³ Companies Act, section 165(7).

⁷⁴ The best interests’ criteria validate the commercial and business reasons for companies declining to pursue derivative claims because the time and resources could be more beneficially used elsewhere. Cassim supra, note 62 at 83-4.

⁷⁵ *Gaiman v National Association for Mental Health* 1970 (2) All ER 362. See also *Contemporary Company Law* at 514-516.

⁷⁶ Maleka F Cassim *The statutory derivative action under the Companies Act of 2008: Guidelines for the exercise of the judicial discretion* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2014) at 73

One author notes that whilst the primary concern is the commercial viability, the strength of the case and its prospects of success are also considered under this test.⁷⁷

Other jurisdictions approach the tests differently. For example, in Canada, the criterion for the ‘best interests of the corporation’ dwells primarily on the strength of the claim as opposed to the commercial viability of the claim.⁷⁸ In addition, the threshold of proof in Canada is lower than the South African and Australian⁷⁹ standards. Section 239(2) (c) of the Canada Business Corporations Act,⁸⁰ only requires that the litigant satisfy the court that the claim ‘appears to be in the best interest of the corporation’.⁸¹ In Australia, the question is whether or not the litigant can establish on a balance of probabilities that the claim is in the best interests of the company.⁸²

Supporting the high threshold for the best interests criterion in South Africa, Cassim argues that minority shareholders, when they wish to act on behalf of the company, must be held to the same standards as directors and officers of the company.⁸³ They must at all times act in the best interests of the company. Thus, the test of the best interests of the company in South Africa, similar to the standard in Australia which the courts have stated, ‘must not be an inquiry into the possibility or potential’⁸⁴ of a claim but that the claim ‘must’ be in the best interests of the company. Cassim argues that if it can be proved that there is an alternative remedy that will provide the same redress and satisfy the notions of justice, then it would not be in the best interests of the court to pursue litigation.⁸⁵ I agree with this reasoning. Litigation should be a last resort after the parties have exhausted all other mediums available to them. As mentioned in chapter one the company is based on a private contract between shareholders. Therefore, where possible, the shareholders must attempt to resolve their disputes without the interference of the courts.

⁷⁷ Cassim supra, note 68 at 73-4.

⁷⁸ Maleka F. Cassim *The statutory derivative action under the Companies Act of 2008: Guidelines for the exercise of the judicial discretion* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2014) at 74.

⁷⁹ Australian Corporation Act section 237(2)(c) ‘it is in the best interests of the company that the litigant be granted leave...’ It appears that the South African criterion of the best interests of the company was modelled after the South African Act.

⁸⁰ Canada Business Corporations Act R.S.C., 1985, c. C-44.

⁸¹ Canadian Business Corporations Act, section 293 (2)(c).

⁸² *Swansson v R A Pratt Properties Ltd 2002 (42) ACSR at 313.*

⁸³ Cassim supra, note 80 at 74. See also Companies Act, section 76(3) which requires directors to act in good faith, for a proper purpose, in the best interests of the company with a degree of care, diligence and skill in the exercise of their duties.

⁸⁴ *Carpenter v Pioneer park Pty Limited (in Liq) 2004 NSWSC 1007 at 19.*

⁸⁵ Maleka Cassim *The New Derivative Action under the Companies Act* (2016) at 84-5.

Although it has been explained that the best interests test is about the commercial viability of a claim, it should not be interpreted, ‘to be a purely “cost-benefit” analysis.’⁸⁶ Hence, even though the monetary value may be inconsequential, the value of deterring future misconduct might prove more important. It has been argued that not only would it be difficult to assess the costs and benefit accurately but the derivative action has more than one purpose. Whilst it is suitable for compensating the company for losses it must be used as a deterrence mechanism.⁸⁷ Others have argued that ‘the derivative action should serve as the principal means by which to enforce the fiduciary duties of corporate officials and to penalise the violation thereof.’⁸⁸

Accordingly, the court must balance the two purposes of compensating the company and deterring the behaviour complained of. The court must not always dismiss an application because the damage is nominal, at the same time some amounts may be too nominal to warrant the involvement of the courts. This paper suggests that in such cases alternative dispute resolution methods must be allowed particularly where they offer cheaper, faster and flexible means of reaching a solution. The courts should be given the discretion to consider other remedies that would achieve justice in a less expensive manner. For example, the list of orders the court can grant when a litigant applies for leave can include the court’s ability to direct the matter for mediation.

Section 166(1) of the South African Companies Act act allows the use of alternative dispute resolution, for example, arbitration, mediation or conciliation instead of the formal courts. It is submitted that this is important for the preservation of business relationships, an element that would be absent if parties pursue the formal court procedures.⁸⁹ Litigation is adversarial in nature and matters before the courts go on public record. With arbitration for example, the matters are closed to the public. However, alternative dispute resolution, whilst more flexible and less procedural, may not always be cheaper than formal courts.⁹⁰ For instance the calling of industry experts and other administrative fees may exponentially increase the costs of alternative dispute resolution.

⁸⁶ Cassim supra, note 70 at 84.

⁸⁷ Cassim supra, note 70 at 84-5.

⁸⁸ John C. Coffee Jr & Donald E. Schwartz ‘The choice of rationales: Deterrence Versus Compensation’ in ‘The Survival of the derivative Suit: An Evaluation and a Proposal for Legislative Reform’ (1981) 81 *Columbia law Review* 261 at 302.

⁸⁹ Steven C. Nelson ‘Alternatives to Litigation of International Disputes’ (1989) Volume 1 *The International Lawyer* pp 187-206 at 188.

⁹⁰ Supra note 89 at 188.

2.5 The issue of costs, checks and balances

The system in South Africa provides for a three-pronged approach that tests the merit of the case before the court can allow the litigant to proceed on behalf of the company. Once it is established that the applicant's case has some merit of consequential benefit to the company, such a litigant should not be impeded by the fear of incurring high litigation costs. It is not in the interests of justice to require the litigant to provide security for costs in derivative actions when, in contrast, such a litigant stands to gain no direct benefit should the case succeed. It is reasonably foreseeable that applicants will be hesitant to cede personal assets without the assurance of a successful outcome. Requiring the litigant to provide security appears to punish persons willing to pursue justice.⁹¹ It, therefore, discourages shareholder awareness and activism. According to section 165(10) and 165(11) of the Companies Act should be amended to repeal the requirement of security for costs from a litigant.

The burden of costs remains one of the greatest impediments to the full use and effectiveness of this derivative remedy. The case of *Wallersteiner v Moir*⁹² made interesting points which South African legislators did not fully appreciate. The *Wallersteiner v Moir* case considered the notion that the company in question should indemnify litigants against costs in the result of a loss since the litigant was acting for the company and not himself.⁹³ The court went further and reinforced the principle that, '... he who would take the benefit of a venture if it succeeds ought also to bear the burden if it fails.'⁹⁴ The same solution and principle presented in *Wallersteiner v Moir* remain valid to date. It is burdensome to request the litigant with a good case to provide personal assets as security for costs yet he or she stands to receive no direct benefit should the case succeed. The request for the security of costs would be better suited to a litigant with a less than satisfactory case that insists on bringing the suit despite the court and company recommendations. The high thresholds required in South Africa provide enough safeguards against frivolous and vexatious claims such that the fear of legal costs should not

⁹¹ Companies Act, section 165(11) provides that the court may require security for costs from a litigant before granting the leave to proceed with the action.

⁹² *Wallersteiner v Moir* 1975 (1) All ER at 849.

⁹³ This was an arrangement between a litigant and a financier, usually a lawyer, to finance the litigation in exchange for a percentage of the award, if the case was won. This was considered illegal as it was considered as a mechanism that encouraged and increased lawsuits.

⁹⁴ *Wallersteiner v Moir* 1975 (1) All ER 849 at 859.

be used as a deterrent mechanism.⁹⁵ Once a litigant has satisfied the court that they are acting in good faith, presenting the trial of a serious question of material consequence to the company and in the best interests of the company, they must be indemnified for the legal costs.

A litigant with an indemnity for costs will neither limit the scope of their investigation into the alleged wrong nor the time they will spend with lawyers and other personnel looking into the matter. However, an indemnity for costs must not be taken as a licence for a litigant to incur exorbitant legal bills. Measures must be put in place so that a litigant will only be entitled to reasonable costs. Any unreasonable costs incurred in excess of what is reasonably acceptable must be borne by the applicant.

2.7 A comparison of the derivative action in Zimbabwe

The newly promulgated Companies and Other Business Entities Act codifies the derivative action under section 60.⁹⁶ This action allows members of the company to sue on a wide basis as read together with sections 54 and 55 of the same Act. Similar to the derivative provision in South Africa, litigants are required by law to make a demand in writing to the directors of the company for the company to sue.⁹⁷ Only after a period of thirty days after this demand is turned down, and all other means have failed, can the applicant approach the courts.⁹⁸ This is a significantly short amount of waiting time in comparison to the sixty days mandated in the South African Companies Act.⁹⁹ However, an applicant's ability to institute a derivative action is dependent on their shareholding.¹⁰⁰ The Companies and Other Business Entities Act only allows for members representing at least ten percent of the voting power to bring a claim before the courts.¹⁰¹ This is very different from the South African Companies Act which allows a broader class of applicants and does not place restrictions based on the amount of shareholding. Whilst the approach in South Africa requires the applicant to first seek leave from the courts to sue, in Zimbabwe the applicant can directly bring an action before the courts. This shortens the process significantly, which can lead to the abuse of this provision leading to an influx of frivolous and vexatious litigation. However, it can be argued that the limitation of the availability of this remedy to only those with ten percent or more of the voting power will

⁹⁵ A discussion above highlights the three tests that a litigant must prove before the courts can grant relief. It is submitted that those tests provide a sufficient method to filter the frivolous lawsuits.

⁹⁶ Companies and Other Business Entities Act, 2018.

⁹⁷ Companies and other business entities section 60 (3) (d).

⁹⁸ Supra note 95.

⁹⁹ Companies Act, section 165 (4) (b).

¹⁰⁰ Companies and Other Business Entities Act, 2018 section 60(2)(c).

¹⁰¹ Companies and Other Business Entities Act, 2018 section 60(2)(c).

drastically reduce the number of cases before the courts. Unlike the South African Act which requires the appointment of an independent investigator to look into the allegation company, the Zimbabwean Act places no such obligation on the company.

Justice Chinhengo in the case of *Westerhoff v Zimbabwe Banking Corporation* emphasised the importance of a litigant furnishing the court with substantial and material information for the court to grant the relief that is being requested.¹⁰² The Judge emphasised that such information has a bearing on whether or not the court grants the order and the failure to do so, willingly or negligently might lead to the failure of the action.¹⁰³ Although the courts recognise the importance of information in establishing one's case, the Companies and Other Business Entities Act does not provide for this right to access company information to shareholders. It is recommended that the new Act include a right of access to information close for shareholders, directors and members of the company as does the South African Act.¹⁰⁴

The Companies and Other Business Entities Act does not provide for the right to resort to alternative dispute resolution prior to formal courts. However, section 61(2) of the same Act allows the court the discretion to make order referring an applicant to proceed with their derivative claim through alternative dispute resolution. This might be possible if the memorandum or articles of association provide for this remedy.

Conclusion

The derivative action in South Africa has fairly been advanced with the abolition of the common law derivative action. The provisions of section 165 of the Companies Act clearly outline the requirements that shareholders must satisfy before the courts can grant them leave to bring a derivative claim. The South African Companies Act has extended legal standing to persons previously unable to bring this claim which extends the application of the remedy to wider group of persons. Furthermore, the South African Companies Act provides a right of access to information to shareholders enabling them to bring substantiated claims, with better prospects of success before the courts. On the other hand, the South African Companies Act places heavy procedural requirements on the minorities, which make litigation seem burdensome. However, minorities are not restricted to the use of formal courts only but may

¹⁰² *Westerhoff v Zimbabwe Banking Corporation* unreported case no. High Court Harare Case No. 105- 2003 at 9.

¹⁰³ *Westerhoff v Zimbabwe Banking Corporation* unreported case no. High Court Harare Case No. 105- 2003 at 11.

¹⁰⁴ Companies Act, section 26.

make use of any form of alternative dispute resolution. This is commendable as it addresses concerns of the burdensome nature of formal court processes.

Chapter 3: Dissenting Shareholder's Appraisal in South Africa

3.1 An introduction to dissenting shareholder's appraisal rights

Dissenting shareholders' appraisal rights, hereinafter referred to as appraisal rights, provide relief in limited circumstances by allowing minority shareholders to withdraw their investment from a company when the company embarks on a direction that is contrary to the minority's liking.¹⁰⁵ The introduction of appraisal rights to South African Company law was influenced by similar provisions from the USA's legal system which can be traced back to Delaware.¹⁰⁶ South Africa adopted and ratified appraisal rights under the current section 164 of the Companies Act. Appraisal rights can be described as a compromise between upholding the majority rule and affording minorities the option to opt out when their business interests are no longer aligned with those of the majority.¹⁰⁷ Appraisal rights provide relief to minority dissenting shareholders facing a buyout by the company allowing them to receive a fair value for their shares.¹⁰⁸ An important aspect of appraisal rights is the question of the valuation of the shares hence the name, appraisal rights.¹⁰⁹ This right is available to shareholders in limited circumstances¹¹⁰ and, as will be demonstrated below, only if the dissenting shareholders follow the procedural requirements strictly.

Appraisal rights provide a statutory exit mechanism in instances where a resolution of fundamental change of the company is proposed and a minority of the shareholders dissent to the adoption of such a resolution.¹¹¹ For instance, when a company contemplates, the alteration of preferences rights and limitations of any class of shares, the disposal of assets, a scheme of arrangement and or a merger or amalgamation, it triggers the application of the appraisal rights.¹¹² Not only do minorities have the right to exit but they do not have to go through the trouble of finding a willing buyer for their shares, the company itself is obligated to buy the

¹⁰⁵Barry M. Wertheimer 'The Shareholder's Appraisal Remedy and how courts determine fair value' (1998) 47 *Duke Law Journal* at 614-615.

¹⁰⁶ New York Code, Model Business Corporation Act and Delaware General Law.

¹⁰⁷ *Cilliers v LA Concorde Holdings Limited & Others* 2018 (6) SA 97 (WCC) at 34.

¹⁰⁸ When a minority section of shareholders is opposed and votes against the adoption of a resolution to implement a fundamental transaction, section 164 of the Companies Act obliges the company to buy the shares of the said minority.

¹⁰⁹ In terms of section 164(14) of the Companies Act, the minority shareholders in this instance can only approach the courts with regard to the valuation of the shares subject to the dissent.

¹¹⁰ Appraisal rights are triggered in three circumstances namely when a company proposes transactions that alter the holding of the company, for example, disposal of assets, scheme of arrangement, amalgamation or merger and amendment of the memorandum of incorporation altering the preferences, rights or limitations or terms of any class of shares.

¹¹¹ *Cilliers v LA Concorde Holdings Limited & Others* 2018 (6) SA 97 (WCC) at 34.

¹¹² Companies Act, section 164(2).

dissenting shareholder's shares.¹¹³ In my view, this is a positive development. It ensures that the board of directors will make every effort to engage in transactions that only further the interests of the shareholders or that if they are looking for a transaction they will do so in good faith and obtain the best deal price for the shares of the company.¹¹⁴

3.2 The justification for appraisal rights

It has been argued that appraisal rights must be treated as an anomaly in corporate jurisprudence and should narrowly be confined and strictly construed.¹¹⁵ There are several justifications for appraisal rights. First, appraisal rights provide a mechanism ensuring that the majority will not disregard the minority's opinion and transform the enterprise at the expense of the minority.¹¹⁶ Secondly, because fundamental changes in the enterprise entail more than a disagreement over business planning, the minority shareholders could have lost a valuable business opportunity causing irreparable harm that cannot be compensated by an opportunity elsewhere.¹¹⁷ Finally, appraisal rights advance the ideals of fairness in the corporation through permitting a shareholder to opt out of a transaction that he or she thinks is ill-considered or unfair and having a ready buyer for their shares.¹¹⁸ Shareholders are protected from being drawn, involuntarily into a drastically different enterprise in which they have no confidence in.¹¹⁹ In essence, appraisal rights involve a delicate attempt at balancing the interests of the majority and minority owners. In summation, 'majority owners should not be chained to what they believe to be an unsound business judgment; yet, neither should the minority owners be bound to remain shareholders when they have similar misgivings.'¹²⁰

¹¹³ Companies Act, section 164(5) entitles dissenting shareholders to place a demand on the company to purchase the dissenting shares.

¹¹⁴ Jaqueline Yeats *The Proper and Effective exercise of Appraisal Rights under the South African Companies Act, 2008: Developing a Strategic Approach Through a Study of Comparable Law* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2015) at 161.

¹¹⁵ Joseph E. Magnet 'Shareholder's appraisal rights in Canada' (1979) 11 *Ottawa Law Review* at 102.

¹¹⁶ Magnet supra, note 122 at 103.

¹¹⁷ Magnet supra, note 122 citing Rams, 'Judicial valuation of dissenting shareholder interests' (1973) 8 *LINCOLN L Rev* 74, at 88.

¹¹⁸ Companies Act, section 164(2) read together with subsection (3).

¹¹⁹ Magnet supra, note 122 citing Eisenberg, 'The Legal Roles of shareholders and management in modern corporate decision-making' 1969 57 *CALIF. L. Rev.* 1, at 80.

¹²⁰ Magnet supra, note 108 citing Lattin, 'Minority and dissenting shareholder's rights in fundamental changes' 23L.

3.3 Explaining the trigger mechanisms for appraisal rights

As alluded to earlier, appraisal rights are only available to shareholders in limited corporate transactions.¹²¹ In South Africa, these are termed fundamental transactions. Fundamental transactions often entail a change in business, a change in ownership or change in the rights of shareholders.¹²² A fundamental transaction occurs when a company is contemplating a merger or amalgamation,¹²³ the disposal of assets,¹²⁴ a scheme of arrangement¹²⁵ or the alteration of the preferences, rights or limitations of any class of its shares.¹²⁶ It is reasonably conceivable that not all shareholders will consent to the proposal and are thus unwilling to continue with their investment in a business that no-longer serves their interest. At the same time, their dissent or disapproval of the proposal does not mean the proposal will be abandoned. When the dissenting shareholders only constitute a minority, steps to implement the transaction will be implemented, triggering the mandatory step requiring the company to buy back its shares from the minority at a fair price. Henochsberg criticises the qualification in section 164(2)(a) that the amendment to the Memorandum of Incorporation must be “materially adverse to the rights or interests as wide and vague”.¹²⁷ The commentators argue that without providing the basis of “rights and interests”, the provision in section 164 can be read to mean other rights and interests outside of the Memorandum of Incorporation. This would result in a wider application of the remedy than the legislators originally intended. Furthermore, section 37(8) gives the remedy if there is an amendment that will materially and adversely alter the preferences, rights, limitations and other terms of a class of shares. The requirement that the alteration must materially and adversely alter is very different from the requirement to materially adversely alter as prescribed in section 164 thus creating an inconsistency in the law.

¹²¹ Companies Act, section 164(2).

¹²² All the fundamental transactions involve the selling of or merging of business interests which affects the ownership and management of the business. The amendment of the MOI can result in the change of rights of shareholders; thus, it is important that shareholders should be allowed to exit the company when the change contemplated is opposite what they contracted to.

¹²³ This is defined by section 1 of the Companies Act as a transaction or series thereof between two or more companies that results in one of the companies being absorbed by the other and taking on the identity of the remaining company or the absorption of the companies under a new company.

¹²⁴ This is understood to mean the sale of fifty percent or more of a company's assets or shares of the company as stipulated in section 112 of the Companies Act.

¹²⁵ This is a proposal by the board of directors of an arrangement between the company and its shareholders relating to any class of securities as stipulated in section 114 of the Companies Act.

¹²⁶ Section 164(2)(a) means that appraisal rights will only apply in cases where the amendment of the MOI is in relation to altering preference rights, or any action that would adversely affect the rights and interests of the holders of such shares.

¹²⁷ Piet Delpont on Henochsberg on the Companies Act 71 of 2008 (2011) at 577.

3.4 Outlining the procedure for asserting appraisal rights in South Africa

When a notice of a special meeting is sent out to the shareholders, it must contain the resolution to be voted on as well as an advisory notice of the shareholders' rights of appraisal of their shares.¹²⁸ The Companies Act does not provide sufficient detail as to the extent of the company's obligation in ensuring that the shareholders fully understand their appraisal rights and how to enforce them. This leaves the provision open to the interpretation of directors who may elect to merely provide a summary of the provisions of section 164 of the Companies Act. It must be understood that the intention of the legislator was to ensure that the company not only performs its due diligence but also that it protects the minority shareholder by informing them of their rights. This applies even in circumstances in which the interests of the company do not coincide with the interests of the minority shareholders. The Canadian Business Corporations Act is similar and instructs that notices of fundamental transactions must also contain notices advising shareholders of their appraisal rights.¹²⁹ However, in Canada, the failure to advise shareholders on these rights does not invalidate the adoption of resolutions voted on.¹³⁰

On receipt of the notice, a shareholder intending to dissent and exercise his or her appraisal rights must send a notice of this intention to the company ahead of the meeting.¹³¹ The dissenting shareholders are required to vote against the resolution.¹³² Section 164 (5) is only available to the dissenting shareholders on condition that they complied with the requirements to serve notice and vote against the resolution.¹³³ There is no flexibility to this rule with regard to allowing shareholders who failed to serve a notice of the intention to vote against the resolution to actually cast a vote on the day.

Once the resolution has been adopted the company must, within ten business days, notify all dissenting shareholders of the adoption of the resolution voted on.¹³⁴ This triggers the shareholder's duty to make a demand for payment or alternatively withdraw their dissent.¹³⁵ A shareholder cannot dissent on a portion of the shares but on all of them.¹³⁶ This is similar to

¹²⁸ Companies Act, section 164(2)(b).

¹²⁹ Canadian Business Corporation Act, sections 189(3), 188 (3)(2)(b), 189(4)(b) & 175(2).

¹³⁰ Canadian Business Corporations Act, sections 189(3), 188(3)(2)(b), 189(4)(b) & 175(2).

¹³¹ Companies, section 164(3).

¹³² Companies Act, section 164(5)(c)(i).

¹³³ Companies Act, section 164(5)(a) & (c).

¹³⁴ Companies Act, section 164(4).

¹³⁵ Companies Act, section 164(4).

¹³⁶ Companies Act, section 164(5).

the Canadian position.¹³⁷ This requirement works as a guard against shareholders who are not opposed to the resolution, in principle but are unwilling to take the full risk, therefore, they split their shares to mitigate the risk.

In making a demand for payment, the shareholder must satisfy the company that they, provided the notice of intention to dissent, voted against the adoption of the resolution, that the company has adopted the resolution voted on and that the shareholder has satisfied all procedural requirements.¹³⁸ Following this, the shareholder must issue a written demand for payment to the company and provide a copy to the 'Takeover Regulation Panel'¹³⁹ and make arrangements to surrender the share certificates to the company.¹⁴⁰

3.5 An analysis of the appraisal rights procedure in South Africa

Access to appraisal rights in South Africa hinges on the shareholder's ability to strictly adhere to the procedural requirements as per the Companies Act.¹⁴¹ Failure to submit a notice or to make a demand within the stipulated time periods will result in the shareholder forfeiting their right.¹⁴² A shareholder is absolved from the obligation to send a notice of objection only if the company did not send a notice of the meeting in the first instance.¹⁴³ The Companies Act places a greater burden on the shareholders than it does on the company. A possible explanation is the fact that it is important for the purposes of commercial strategy and planning for the directors to know how many shareholders will dissent to a proposal.¹⁴⁴ In terms of the Model Business Corporation Act 2016 (MBCA), if the company does not respond or commence an action for the courts to determine the fair value within a stipulated time period, the MBCA requires the

¹³⁷ Canadian Business Corporation Act, section 190 (4). Procedure as discussed above at para 3.4.

¹³⁸ Companies Act, section 164(5)(a), (b), (c)(i)(ii).

¹³⁹ This is an organ established in terms of section 196 of the Companies Act with a broad range of functions. The panel regulates fundamental transactions within corporations and ensures the protection of minority shareholders.

¹⁴⁰ Companies Act, section 164(8) requires the shareholder to deliver copies of the demand of payment for fair valuation to the Takeover Regulation panel with details of the shareholder's name and address, the number of shares in respect of which the shareholder seeks payment and the demand for payment of the fair value of those shares.

¹⁴¹ Companies Act, section 164(5) states that a shareholder can only make a demand for payment if the shareholder gave the company notice of objection, the shareholder voted against the resolution and followed all of the procedural requirements.

¹⁴² Companies Act, section 164(7) the shareholder must make a demand on the company within twenty days of receiving a notice from the company on the adoption of the resolution or within twenty days of learning of the adoption of the resolution.

¹⁴³ Companies Act, section 164(6).

¹⁴⁴ Jaqueline Yeats 'The Proper and Effective exercise of Appraisal Rights under the South African Companies Act, 2008: Developing a Strategic Approach Through a Study of Comparable Law' (unpublished Doctor of Philosophy thesis, University of Cape Town, 2015) at 161.

company to pay the shareholder the demanded price per share.¹⁴⁵ This ensures that the company will act swiftly to the demands of the shareholders and the procedural burden is shared equally. It is recommended for South Africa to consider adopting such a provision to ensure that companies have an incentive to adhere to the procedure, particularly the timelines.

If a shareholder accepts an offer from the company, all their rights in relation to the shares subject to the appraisal are immediately suspended.¹⁴⁶ The Companies Act does not provide for compensation to the shareholder for the loss of opportunity during the time between the demand for payment and receipt of payment. Due to the inability to access their capital, pending the outcome of the litigation, the minority may miss out on other investment opportunities. Although the court has the discretion to consider all relevant facts in determining the fair value and on whether to grant an order of interest or not the concept of lost opportunities may not be considered.¹⁴⁷

Although the entire procedure is strict, it is accepted that procedures exist as a management tool to avoid frivolous suits. For example, minority shareholders can decline a fair offer on their shares and engage on a meritless suit in a bid to stall the implementation of the deal.¹⁴⁸ Nevertheless, there must be an equitable balance to ensure that the procedure does not inadvertently become a barrier to applicants seeking help.

Any rigid procedure that cannot be deviated from must have a justification, a principle or interest that it seeks to protect. The notice of intention to dissent in the company's planning and forecasting is an important feature.¹⁴⁹ Before voting on the contemplated transaction, the directors must have, based on responses received from notices, a clear picture of the support they have for the transaction and the number of shareholders opposing it.¹⁵⁰ This will assist in planning the financial requirements towards paying dissenting shareholders, negotiating better terms of the deal and it could be an indicator of whether or not the company needs to withdraw

¹⁴⁵ Model Business Corporations Act, section 13.30 (a).

¹⁴⁶ Companies Act, section 164(9).

¹⁴⁷ Companies Act, section 164(15)(c)(iii)(bb).

¹⁴⁸ Yeats *supra*, note 157 at 161 J. Yeats states that the view of the corporate leadership is that the appraisal rights do not protect corporation from demands motivated by the hope of a nuisance settlement or fanciful conceptions of value.

¹⁴⁹ Jacqueline Yeats *'The Proper and Effective exercise of Appraisal Rights under the South African Companies Act, 2008: Developing a Strategic Approach Through a Study of Comparable Law'* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2015) at 162. The company has no way of determining how many shareholders will dissent to a fundamental transaction. That results in the company's inability to plan ahead. The requirement of the notices is the first chance the company gets of understanding how receptive the shareholders are of the appraisal.

¹⁵⁰ Yeats *supra*, note 162 at 162.

from the transaction.¹⁵¹ Inability to know how many shareholders will dissent can possibly destabilise the implementation of the proposed transaction.¹⁵² A new practice that has emerged is that lawyers advise their corporate clients to incorporate clauses that will allow them to withdraw from a contract should the number of dissenting shareholders exceed projections.¹⁵³

Although the court's involvement is minimum¹⁵⁴ in my view the procedure between the company and the shareholders outside of the courts can be made more flexible. For example, the legislature may allow dissenting shareholders grace periods to file late process. This will allow dissenting shareholders who lack the legal training to make an informed decision and to decisively act. However, the grace or condonation periods must be strict to ensure that they are not prone to abuse or used as a tactic to prevent the implementation of the proposed transaction. This can be achieved by limiting the grounds on which late filing of documents may be condoned.

3.6 The approach to determining 'fair valuation' of dissenting shares

Once the proposed transaction has been adopted, the dissenting shareholders must make a demand on the company to be paid the fair value of their shares.¹⁵⁵ The Companies Act does not define what fair valuation is nor does it place a mandate on the company to reveal to the dissenting minority the calculation method that was employed to arrive at a given value. If the shareholders disagree with the valuation of their shares, they can approach the courts for a determination in terms of section 164(14) of the Companies Act.

It is interesting to note that there is no fixed method of determination. However, the courts can enlist the assistance of appraisers who are normally experts in the field to arrive at what would be considered a fair price for the shares.¹⁵⁶ The appointment of the expert is done at the discretion of the court and without consulting the parties affected.¹⁵⁷ The question of which method to apply or what factors are considered in arriving at a fair valuation is not settled. It

¹⁵¹ Yeats supra, note 162 at 162.

¹⁵² The case of *Juspoint Nominees (Pty) Limited & Others v Sovereign Food Investments Limited & Others* 2016 All (SA) at 15 is a case example of where a fundamental transaction had to be abandoned because the number of dissenting shareholders exceeded the board's expectations.

¹⁵³ Yeats supra, note 162 at 167.

¹⁵⁴ The court is only involved at the end of the process for the determination of the fair, provided that the parties are not in agreement. The company or the shareholder only rely on the courts after failing to reach a mutual agreement on the valuation of the shares.

¹⁵⁵ Companies Act, section 164(5), (7) & (8).

¹⁵⁶ Companies Act, section 164(15)(c)(iii)(aa).

¹⁵⁷ Section 164(15)(iii).

has been maintained that although the question of fair valuation has been determined in dealing with oppression remedy the same cannot be applied to appraisal rights.¹⁵⁸ This is because under the oppression remedy the courts will be dealing with a willing buyer whilst in appraisal rights, the buyer is an unwilling one.¹⁵⁹ It is difficult to impress upon the provision of a list of calculation methods or factors because each case is different. The value of the shares is determined as at the date on which, and the time immediately before the company adopted the resolution that gave rise to the appraisal rights. However, that does not mean the company or the courts will take into account the effect of the resolution. Henochsberg declares that the effect (positive or negative) of the event that triggered the appraisal rights is not considered in the calculation of fair value because the dissenting shareholders did not approve it.¹⁶⁰ It is left to the courts and the expert to calculate the value of the shares based on the surrounding factors. The onus therefore is on each party to convincingly argue which factors must and must not be considered or which method is appropriate.

Once a price has been determined, the courts may make an order of interest at a reasonable rate to be calculated from the date the resolution became effective to the date of full and final payment.¹⁶¹ Courts are lenient to allow companies who would risk falling to insolvency if called upon to make all appraisal payments at once to instead enter into payment plans.¹⁶² This will guarantee the continuity of the business at the same time enable the company to meet its obligations. The solvency and liquidity¹⁶³ of the company is a consideration the courts must consider in determining the fair value.¹⁶⁴

3.7 The burden of the costs of suit

The Companies Act provides that the court, ‘may make an appropriate order of costs, having regard to any offer made by the company and the final determination of the fair value by the

¹⁵⁸ Jaqueline Yeats *The Proper and Effective exercise of Appraisal Rights Under the South African Companies Act, 2008: Developing a strategic approach through a study of comparable law* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2015) at 170.

¹⁵⁹ *Contemporary Company Law* at 809.

¹⁶⁰ Piet Delport Henochsberg on the Companies Act 71 of 2008 (2011) at 577.

¹⁶¹ Companies Act, section 15(c)(iii)(bb).

¹⁶² Companies Act, section 17 (a) & (b) (ii). Furthermore, the court may allow the company to pay the due amount in instalments should the company prove that a once off payment will hinder it from its commitment to other obligations. This is not a disregard of the shareholders’ right to their capital investment but a means of ensuring that the company remains solvent. This can be applicable where there is large number of dissenting rights.

¹⁶³ Companies Act, section 4(1) states the company would have established its solvency and liquidity if it can prove to the court that its assets exceeds its liabilities and that it will be able to pay its debts as they become due and payable within a period of 12 months from the date the test is considered.

¹⁶⁴ Companies Act, section 17(b)(i).

court.¹⁶⁵ The results will be that if the court determines the fair value to be considerably higher than the offer of the company, the court may award costs in favour of the shareholder and the opposite applies.¹⁶⁶ In terms of the MBCA, the company will bear the burden of court costs¹⁶⁷ for both parties (different from legal costs) together with the company's legal costs and may depending on the court, have to pay the shareholders' legal costs.¹⁶⁸ This approach will lessen the burden on the shareholders who only have to pay for their lawyers. However, appraisal litigation can be complex and require teams of legal experts in the relevant field and this may not be practical for an individual shareholder. This could leave dissenting shareholders with no option but to abandon any aspirations to pursue their rights, even if they have a rightful claim. Thus, whilst the remedy is available, the cost of exercising the right may ultimately render it unattainable for some minority shareholders. Minorities may elect to pursue any of the three forms of arbitration

3.8 Zimbabwe and the introduction of appraisal rights

The newly promulgated Companies and Other Entities Act provides for dissenting shareholders' appraisal rights.¹⁶⁹ The appraisal rights will be applicable in similar circumstances to the South African Companies Act instances namely, a variation of rights attached to any shares¹⁷⁰ mergers and amalgamations¹⁷¹ and major asset transactions.¹⁷² Section 95(8) of the Zimbabwean Companies and Other Business Entities Act separately makes provision for the application of appraisal rights. This section is strikingly similar to the South African provision under section 37(8) of the Companies Act. Whilst the above mentioned clauses are similar word for word, the same cannot be said for parallel provisions namely section 232 of the Zimbabwean Companies and Other Business Entities Act and section 164 of the South African Companies Act. For example, the application of appraisal rights in

¹⁶⁵ Companies Act, section 164(15)(iv).

¹⁶⁶ Jaqueline Yeats *The Proper and Effective exercise of Appraisal Rights Under the South African Companies Act, 2008: Developing a strategic approach through a study of comparable law* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2015) at 204.

¹⁶⁷ These are defined as expenses charged in a law suit as determined by the courts. Whereas legal costs relate to the parties' cost in hiring attorneys and expert witnesses.

¹⁶⁸ Model Business Corporation Act, section 13.31(a).

¹⁶⁹ Companies and Other Business Entities Act, 2018 section 232.

¹⁷⁰ Companies and Other Business Entities Act, 2018 section 141(1).

¹⁷¹ Means the merging of one or more existing companies into another existing company as defined by section 225 of the Companies and Other Businesses Entities Act.

¹⁷² Means a transaction or related series of transactions involving the purchase, sale, transfer, pledge or mortgage outside the usual course of the company's business as defined by section 225 of the Companies and Other Business Entities Act, 2018 section.

relation to the amendment of the memorandum or articles has a narrow application. The Zimbabwean provision in section 232 of the Companies and Other Business Entities Act does not qualify that there be a “materially adverse” effect on the rights and interests of the shareholders in order for the variation to trigger appraisal rights.

The procedural formalities required of dissenting shareholders in Zimbabwe are also very similar to its South African counterpart. The clause also provides for litigation in the event that the shareholders and the company are unable to come to an agreement on what is the fair value of the shares.¹⁷³ The courts are given latitude and will have the discretion to consider various factors in determining the fair value. Having a strict formula can be difficult if there are unforeseen circumstances that arise and contribute to the determination of fair value.

Conclusion

Appraisal rights are an important part of protecting dissenting minorities by guaranteeing them the protection of their rights and when that is threatened to change, they are allowed to exist the business. By mandating the company to purchase the dissenting shares at a fair value, both the South African Companies Act and the Zimbabwean Companies and Other Business Entities Acts protect minorities who would otherwise have no negotiating leverage if they were to seek their own buyers. Both Acts mentioned above also balance the need for the company to plan ahead by placing heavy procedural burdens on the minorities together with penalties for failure to adhere to these procedures. However, the company does not face similar penalties and this produces an imbalance in the provision. It is recommended that this must be rectified by placing similar penalties on the company to incentivise the company to adhere to the procedural requirements. The involvement of the courts is kept to a minimum by only invoking their involvement at the valuation stage in instances where the parties disagree.

¹⁷³ Companies and Other Business Entities Act, 2018 section 232.

Chapter 4: The evolution of the oppression remedy in South Africa

4.1 A discussion of the oppression remedy

The cardinal rule in company law is that the management of the business and affairs of a company is under the direction of the board of directors which has full authority.¹⁷⁴ The shareholders surrender the management of the company to the directors who are duty bound to act diligently and in the best interests of the company.¹⁷⁵ The courts have famously upheld that the directors are best positioned to fulfil their mandate and the courts try to refrain from questioning the wisdom of the directors' decisions.¹⁷⁶ The courts precisely explained this point in the case of *Louw v Nel* at 678 G-H stating minority shareholders, in terms of the contract they signed are bound by the decisions of the majority, even where such decisions adversely affect the minority, for as long as such corporate decisions are arrived at in accordance with the law. The supremacy of the majority is essential to the proper functioning of companies.¹⁷⁷

However, the authority of the board does not go unchecked. The law provides a checks and balance mechanism to prevent the abuse of the authority given to directors in section 66 of the South African Companies Act mentioned above. A remedy is available to shareholders and directors who complain of, have been or continue to face oppressive or unfairly prejudicial conduct¹⁷⁸ from majority shareholders and other members of the company.¹⁷⁹ This remedy is known as the oppression remedy as provided for by section 163 of the Companies Act. In South Africa, the oppression remedy is available to two specific groups of persons namely,

¹⁷⁴ Companies Act, section 66(1).

¹⁷⁵ Section 76 of the Companies Act places several obligations on directors to name a few, the duty to act in the best interests of the company, the duty to exercise a degree of care, skill, and diligence, the duty to act in good faith and for a proper purpose in carrying out their functions.

¹⁷⁶ Maleka F Cassim *The statutory derivative action under the Companies Act of 2008: Guidelines for the exercise of the judicial discretion* (unpublished Doctor of Philosophy thesis, University of Cape Town, 2014) at 73. Although this concept was explained in the context of the derivative action it bears the same meaning in this case.

¹⁷⁷ *Louw & Others v Nel* 2011 (2) All SA at 172 (SCA) at 22 citing *Sammel v President Brand Gold Mining Co Ltd* 1969 (3) SA 629 (A) at 678 G-H.

¹⁷⁸ Although the Companies Act does not provide a definition, this is understood to mean a variety of action that entail the abuse of one's power and duty to the detriment of others. The terms will be discussed in more detail below.

¹⁷⁹ Companies Act, section 163.

shareholders and directors.¹⁸⁰ However, in other jurisdictions, such as Canada, there is no restriction as to who can approach the courts for relief from oppressive conduct.¹⁸¹

The nature of the oppression remedy is to provide relief to shareholders or directors who are subjected to oppressive or prejudicial conduct or the abuse of the separate legal personality of the company.¹⁸² The remedy is distinguished from the derivative action because the litigants approach the courts in their personal capacity and not on behalf of the company although the company as a whole might benefit from the suit. Aggrieved shareholders can bring before the court's complaints of practices, decisions and any other conduct of persons that has had an unfairly negative impact on their interests.¹⁸³

4.2 A look at the legal standing for the remedy

Section 163(1) of the Companies Act provides that a shareholder or director may approach the court for relief from conduct that is oppressive, unfairly prejudicial or the abuse of separate juristic personality of the company that has an unfairly negative impact on their interests. Cassim highlights that the expansion of the legal standing to include directors therefore means the oppression remedy now applies to quasi-partnerships which historically brought the highest cases of oppression allegations.¹⁸⁴ Related persons can now sue under the oppression remedy, this means shareholders or directors of holding or subsidiary companies may also complain about the conduct of affairs of a subsidiary or holding company respectively.¹⁸⁵ Whilst the extension of legal standing to include directors and shareholders is an improvement from the old (1973) Companies Act, in comparison to other jurisdictions, South Africa can further improve. In contrast, Australia¹⁸⁶ and Canada¹⁸⁷ provide an extensive list of persons who can

¹⁸⁰ Companies Act, section 163(1).

¹⁸¹ Canada Business Corporations Act section 241 (1).

¹⁸² Section 163(2) of the Companies Act provides a lengthy and open-ended list of remedies available to shareholders. Such remedies range from compensatory orders, ordering issues of contention to trial, appointing directors amongst other remedies. These will be more fully discussed in later chapters.

¹⁸³ Although the Companies Act does not define the term interests, case law has defined to mean more than a shareholders' legal rights and extends to relations of the company with third parties.

¹⁸⁴ *Contemporary Company Law* at 760.

¹⁸⁵ *Supra* note 177. See also *Contemporary Company Law* at 767.

¹⁸⁶ Australia Corporation Act of 2001, section 234 of the Act stipulates that the remedy is available to the following class of persons; persons to whom a share in the company has been transmitted by will or by operation of law or persons whom the Australian Securities and Investments Commission thinks appropriate, former members of the company and those removed from the register of members.

¹⁸⁷ The Canada Business Corporations Act (hereafter referred to as the CBCA), section 238 defines a litigant as, a registered holder, beneficial owner and a former registered holder or beneficial owner of a security of a corporation and its affiliates. A director or an officer or a former director or officer of a corporation or any of its affiliates the director or any other persons who in the discretion of the court, is a proper person to make an application under the said provision.

apply to the courts for relief under the oppression remedy. In addition, the courts in Australia and Canada have the discretion to grant legal standing to any person the courts deem as ‘proper’ person to make the application.¹⁸⁸ This ensures that the courts can protect, employees, investors and other stakeholders who may have interests in a company. The availability of the oppression remedy to more litigants is commendable because it recognises that, there other stakeholders with interests in how the company is managed who can be protected by the oppression remedy.

4.6 Discussion of factors qualifying for the oppression remedy

The result of conduct

In terms of the Act, The conduct complained of must be completed and manifest a result that is oppressive, unfairly prejudicial or unfairly disregards the interests of the shareholders.¹⁸⁹ The courts have emphasised that it is the result and not the act that must be oppressive or unfairly prejudicial.¹⁹⁰ The effect of this that shareholders are precluded from approaching the courts for relief for an anticipated wrong. For example, the board may call for a vote on a proposal that will adversely affect the interests of minorities and unfairly so. In terms of the current provisions, the minorities cannot approach the courts to prevent this from happening but must await the implementation and effect of the said proposal. However, shareholders should be allowed to approach the court for an order preventing the act.¹⁹¹

4.6.1 Towards the definition of oppressive conduct

Although the Companies Act has shied away from providing a definition of oppressive conduct, case law has attempted to provide clarity on what qualifies as oppressive conduct. There is a wide spectrum or field in which oppressive conduct may fall. Courts have defined it as conduct that is any of the following; burdensome, harsh and wrongful, a clear departure from the standards of fair dealing and abuse of power which results in a lack of confidence in the manner in which the affairs of the company are being conducted.¹⁹² South African courts have defined oppressive conduct as conduct that is unjust, harsh or tyrannical.¹⁹³ In other instances,

¹⁸⁸ The Australian Corporations Act 2001, section 234(e) and the Canada Business Corporations Act, section 238(d).

¹⁸⁹ Companies Act, section 163(1)(a).

¹⁹⁰ Cassim supra, note 199.

¹⁹¹ *Contemporary Company Law* at 765.

¹⁹² *Scottish Co-Operative Wholesale Society Ltd v Meyer* 1958 (3) All E.R. 66.

¹⁹³ *Grancy Property Limited v Manala & Others* 2013 (3) All SA 111 (SCA).

it is described as conduct that lacks probity or fair dealing or that is a visible departure from the standards of fair dealing.¹⁹⁴ Conduct that violates the conditions of fair play on which every shareholder who entrusts his money to a company is entitled to rely on has also been held to be oppressive conduct.¹⁹⁵ As mentioned above, there is a wide spectrum of definitions and the courts have also acknowledged that these definitions are widely divergent.¹⁹⁶ This is to say that the definitions of oppression are on either end of the spectrum. Conduct that is tyrannical is different from conduct that consists of a violation of the conditions of fair play.¹⁹⁷ Due to the different definitions of the word oppressive, it has become difficult to easily identify the accurate meaning of the word. The lack of a precise meaning of the word leads to difficulty in assessing what can be classified as oppressive conduct. The court answered this question in the case of *Aspek Pipe v Maurerberger* stating that a litigant should not have to go to the lengths of establishing the conduct of a tyrannical nature before they are entitled to relief under section 163.¹⁹⁸ In essence, the term oppressive conduct can be construed to mean all of the mentioned types of conduct, but the litigant will not be required to establish tyrannical actions to obtain relief as that is a higher form of oppression.

4.6.2. Towards the definition of unfairly prejudicial, unfairly disregards interests

If the conduct complained of does not amount to oppressive conduct, litigants may still sue for conduct that is unfairly prejudicial or that unfairly disregards their interests.¹⁹⁹ However, not all conduct that is prejudicial is unfair.²⁰⁰ The company may make decisions, for example, not paying dividends to shareholders which is prejudicial to their interests but may have valid justifications for doing so. Therefore, the conduct complained of must be both prejudicial and unfairly so to the litigant.²⁰¹ A successful application must satisfy both of these elements.²⁰² It

¹⁹⁴ *Omar v Inhouse Venue Technical management (Pty) Limited and Others* 2015 (3) SA 146 (WCC) at 4.

¹⁹⁵ Ferdinand S. Tinio 'What amounts to "Oppressive" conduct under statute. Authorising Dissolution of Corporation at suit of minority stockholders', (2016) 56 A.L.R 3D 358. 2.

¹⁹⁶ *Grancy Property Limited v Manala & Others* 2013 (3) All SA 111 (SCA).

¹⁹⁷ *Grancy Property Limited v Manala & Others* 2013 (3) All SA 111 (SCA).

¹⁹⁸ *Aspek Pipe Co (Pty) v Maurerberger* (1968) (1) (SA) 517 (C) at 525H-526E.

¹⁹⁹ The Companies Act provides that a litigant may sue on either of the three circumstances. The law does not mandate that all three circumstances must be alleged in one action.

²⁰⁰ The Henochsberg on the Companies Act 71 of 2008 (2011) at 574 explains that not all corporate decisions made will favour all shareholders. Every shareholder who votes against a resolution may consider the implementation of that resolution as prejudicial. However, this may not be unfair particularly where all the procedures have been observed. The litigant would have to prove the unfairness.

²⁰¹ United Kingdom Law Commission Consultation Paper (CP 142) Shareholder Remedies citing Peter Gibson J in re Ringtower Holdings plc 1989 (1) BCLC 427. 437.

²⁰² Edward B. W. Tong 'A departure from the majority rule: unfair prejudice in the Companies' Ordinance (cap.622) available at http://www.hkiaat.org/e-newsletter/Oct-15/technical_article/PBEIV.pdf citing Re Saul D Harrison & Sons plc 1995 (1) BCLC 14, accessed on 28 January 2019.

is not sufficient for the alleged conduct to satisfy only one of these elements.²⁰³ ‘Thus not all acts which prejudicially affect shareholders or directors, or which disregard their interest, will entitle them to relief- it must be shown that the “conduct” is not only prejudicial or disregarding but also that it is unfairly so’²⁰⁴

Courts have also stated that keeping promises and upholding agreements is important in maintaining commercial fairness.²⁰⁵ Thus, for any investigation into unfair conduct, it would be prudent to begin the investigation with a comparison of the alleged conduct *vis-a-vis* the terms of the MOI.²⁰⁶ In essence, unfairness refers to conduct that departs from or abuses the agreed terms and any conduct that goes against principles of equity.²⁰⁷ The litigant must prove that the conduct has damaged or seriously jeopardised the value of his or her interest within the company.²⁰⁸ Additionally, they must prove that the same conduct has caused damage to the financial interests of the members such as the devaluation of shares. The conduct complained of can manifest in various ways, such as infringement of rights stipulated in the MOI and the misappropriation of company funds.²⁰⁹

The innovative insertion of interests means that an applicant can sue for conduct even when it does not violate their rights.²¹⁰ However, the Companies Act does not provide a definition of the ‘interests’. Cassim proposes that in the absence of such definition the courts will have to take into account equitable considerations such as shareholders’ legitimate expectations arising from collateral agreements.²¹¹ In *Count Gotthard SA Pilati v Witfontein Game Farm (Pty) Ltd*, interests were defined as to arise out of fundamental understanding between the shareholders, which forms the basis of their association but was not in contractual form.²¹²

²⁰³ Edward B. W. Tong ‘A departure from the majority rule: unfair prejudice in the Companies’ Ordinance (cap.622) available at http://www.hkiaat.org/e-newsletter/Oct-15/technical_article/PBEIV.pdf citing *Re Saul D Harrison & Sons plc* [1995] 1 BCLC 14, accessed on 28 January 2019.

²⁰⁴ *Contemporary Company Law* at 771-2.

²⁰⁵ United Kingdom Law Commission Consultation Paper (CP 142) Shareholder Remedies at 78.

²⁰⁶ United Kingdom Law Commission Consultation Paper (CP 142) Shareholder Remedies at 78.

²⁰⁷ Edward B. W. Tong ‘A departure from the majority rule: unfair prejudice in the Companies’ Ordinance (cap.622) available at http://www.hkiaat.org/e-newsletter/Oct-15/technical_article/PBEIV.pdf at 3, accessed on 28 January 2019.

²⁰⁸ United Kingdom Law Commission Consultation Paper (CP 142) Shareholder Remedies at 81.

²⁰⁹ Edward B. W. Tong ‘A departure from the majority rule: unfair prejudice in the Companies’ Ordinance (cap.622) available at http://www.hkiaat.org/e-newsletter/Oct-15/technical_article/PBEIV.pdf citing *Re Elgindata Ltd* [1991] BCLC 959. Accessed on 28 January 2019.

²¹⁰ *Contemporary Company Law* at 770.

²¹¹ *Contemporary Company Law* at 770.

²¹² *Count Gotthard SA Pilati v Witfontein Game Farm (Pty) Ltd and Others* [2013] 2 All SA 190 GNP at 17.4.

4.7 Considering the possible court orders

Once a court is satisfied that the business of the company has been conducted in an unfairly prejudicial or oppressive manner, it is empowered to make a final or interim order as it considers fit.²¹³ The wide powers are a welcomed addition as they that ensure the courts have room to make decisions that are fair, equitable and appropriate in consideration of all the circumstances and the parties in the case. The court has to be able to cure the unfair prejudice suffered at the hands of the majority.²¹⁴ In the case of *Lourenco v Ferela*, the court stated that it is essential for the litigant to formulate the relief that they are seeking,²¹⁵ but the court is not limited by the applicant's formulation of the relief sought.²¹⁶ In doing so, it will streamline the points of argument, provide clarity and direction to the courts and increases the prospects of success for the claim. However, the lists are not exhaustive and the courts, through the discretion granted to them may structure a form of relief that fits the circumstances of the particular case at hand.²¹⁷ Although section 163 of the Companies Act does not require the litigant to come before it with clean hands, the actions of the minority shareholder leading to the dispute in question will be considered. If the fault can be established on the part of the litigant, the courts will take that into consideration when granting the relief.²¹⁸ Therefore the conduct of the litigant may have a negative impact on the type of relief the court will grant.

Needless to say, any relief granted must be commensurate to the conduct subject to the complaint. In *Louw v Nel*, the court emphasised that the nature of the remedy that the court will grant will depend upon the conclusion on the degree of oppression but the court must also strive to achieve fairness on both sides.²¹⁹ The court order must be sufficient to solve the problem and be feasible to implement.

The South African list of remedies is extensive,²²⁰ much like the Canadian²²¹ and Australian²²² provisions. The oppression remedy provides relief that entails both the minimal as well as

²¹³ Companies Act, section 163 (2) states that, 'upon considering an application in terms of subsection (1), the court may make any interim or final order it considers fit...'

²¹⁴ *Louw v Nel* 2011 (2) SA 172 (SCA) at 21.

²¹⁵ *Lourenco v Ferela (Pty) Ltd* (No1) 1998 (3) 281 (T) at 295-6.

²¹⁶ *Heckmair v Beton & Sandstein Industries' (Pty) Ltd* (1) 1980 (1) SA 350.

²¹⁷ Companies Act, section 163(2) gives the courts the power to grant any interim or final it may deem fit. This means it is left to the court to determine what is best for the parties in the circumstance.

²¹⁸ *De Sousa and Another v Technology Corporate Management (Pty) Ltd & Others* 2017 (3) All SA 47 at 52.

²¹⁹ *Louw v Nel* 2011 (2) SA 172 (SCA) at 31.

²²⁰ Section 163(2) and *Off-Beat Holiday Club & Another v Sanbonani Holiday Spa Share Block Ltd & Others* 2017 (7) BCLR 916 at 574.

²²¹ Canada Business Corporation Act, section 241(3).

²²² Australia Corporations Act 2001 section 233(1).

intrusive involvement of the courts trumping the principle of minimal judicial interference in the management of the company.²²³ Some of the remedies shift and change the power structures of the company, for example, the appointment of new directors, amendment of the MOI and the issuing and exchange of shares.²²⁴ Accordingly, courts must guard against oppressing the majority with the use of extreme relief measures. Commentators have warned that these wide powers conferred upon the courts must be carefully controlled to prevent turning the oppression remedy into a source of abuse itself.²²⁵

In conclusion, before a court can grant the relief petitioned by the litigant, the litigant must establish the following, that the alleged has been committed, that the conduct or act is unfairly prejudicial, unjust or inequitable to them or some part of the members of the company.²²⁶ In addition, the litigant must prove that the nature of the relief being sought will cure the nature of the conduct complained of and that it is just and equitable that the relief is granted.²²⁷

4.8. The oppression remedy in Zimbabwe and the procedure

Section 222 of the Companies Act restricts the availability of the oppression remedy only to members²²⁸ of the company. In Zimbabwe, case law has clarified the question of who qualifies to use the oppression remedy.²²⁹ In the case of *Zvandasara v Saungwemwe*, the courts made it clear that only shareholders and members of the company may apply to the courts for relief from oppressive or unfairly prejudicial conduct.²³⁰ It was reinforced that legal standing is only available to, shareholders and members and not those acting in some other capacity such as that of a director, servant, employee or agent of the company.²³¹ In dismissing the application of a director alleging oppression, the court stated that the complaints of a director were an employment matter belonging in the labour realm and should be dealt with separately from his

²²³ Companies Act 71 Of 2008 Section 163(2).

²²⁴ Companies Act 71 of 2008 Section 163(2)(c)(d)(e)(f).

²²⁵ MS Blackman in Commentary on the Companies Act Volume 2 (2002) at 9-4.

²²⁶ Companies Act 71 of 2008 Section 163(2).

²²⁷ *Grancy Property v Manala & Others 2013 (3) All SA 111 (SCA) at 120.*

²²⁸ Zimbabwe Companies Act Chapter 24:03. Section 221 defines members for the purposes of section 222 as persons who are not members of the company but to whom shares in the company have been transferred or transmitted by operation of law.

²²⁹ *Zvandasara v Saungweme & Others* unreported judgment case no. HH 108 of 2018 at 5. See also, *Aspek Pipe Co (Pty) Ltd v Mauerberger* 1968 (1) SA 517 (C).

²³⁰ *Zvandasara v Saungweme & Others* unreported judgment case no. HH 108 of 2018 at 5. See also, *Aspek Pipe Co (Pty) Ltd v Mauerberger* 1968 (1) SA 517 (C).

²³¹ *Zvandasara v Saungweme & Others* unreported judgment case no. HH 108 of 2018 at 5. See also, *Aspek Pipe Co (Pty) Ltd v Mauerberger* 1968 (1) SA 517 (C).

rights as a shareholder.²³² However, this reason was flawed. If an employee can establish a pattern of behaviour that highlights the intention to oppress them as a shareholder, the courts must be open to hearing a case of that nature. This provision is unnecessarily restrictive and does not advance the protection of minority shareholders. The unfortunate effect of such restrictive application was illustrated in Henochsberg highlighting that, in quasi-partnerships, shareholders will take up directorship positions in the company and opt to receive the return on their investment as remuneration.²³³ If the minority shareholders are denied this remuneration, the courts must allow them recourse to sue either in their capacity as directors.²³⁴

It is recommended that the legislators should make every attempt to advance rather than restrict the functions of this remedy by broadening the list of persons qualifying to, at the very least, include directors and other officers of the company as is the case in South Africa.²³⁵

Unlike the South African Companies Act, which requires the result of the conduct as grounds or cause of action, the Zimbabwean Companies Act allows applicants to institute action on the basis of a proposed action that they deem could have oppressive effect on their interests.²³⁶ In this regard the Zimbabwean Companies Act opens up this remedy to be both preventative and reactionary.

Regarding the procedural requirements, the litigant must prove that he or she is a shareholder or a member of the company, that they are oppressed, that the oppression is at the hands of another member of the company and that the oppressive conduct is in relation to the conduct to the affairs of the company.²³⁷ The details of the complaint must be set out in the application documents with specific details of how the affairs of the company are being conducted in a manner that is oppressive or prejudicial to them.²³⁸ The court will not grant relief that is based on generalised averments of said oppressive conduct²³⁹, a litigant must allude to specific incidents for a specific case. In an effort to maintain its distance from the internal management of a company, the courts will only intervene in exceptional circumstances provided for in the

²³² *Zvandasara v Saungweme & Others* unreported judgment case no. HH 11342/14 at 6.

²³³ Piet Delport Henochsberg on the Companies Act 71 of 2008 (2011).

²³⁴ Piet Delport Henochsberg on the Companies Act 71 of 2008 (2011) at 575.

²³⁵ Companies Act, section 163(1).

²³⁶ Companies and Other Business Entities Act, 2018 section 222.

²³⁷ *Zvandasara v Saungweme & Others* unreported judgment case no. HH108 of 2018 citing *Marshall v Marshall (Pty.) Ltd & Others*, 1945 (3) SA. 571 (N).

²³⁸ *Zvandasara v Saungweme & Others* unreported judgment case no HH citing *Livanos v Swartzberg & Others* 1962 (4) SA 395 (W.L.D at 397 A-D).

²³⁹ *Zvandasara v Saungweme & Others* unreported judgment case no. HH 108 of 2018 citing *Livanos v Swartzberg & Others* 1962 (4) SA 395 (W.L.D at 397 A-D).

Zimbabwean Companies Act.²⁴⁰ Consequently, the litigant must prove to the court that such circumstances are present for the courts to intervene.

In a similar fashion to the South African Companies Act, the Zimbabwean Companies and Business Entities Act, gives wide discretionary powers to the courts to make orders fitting to each particular case.²⁴¹ This is a welcome change from its predecessor Companies Act Chapter 23:04 which prescribed a limited list of available remedies. Furthermore, section 61 of the Companies and Other Business Entities Act provides other orders that the courts are allowed to make to relieve applicants. Although the Zimbabwean Companies Act allows for non-binding alternative dispute resolution,²⁴² the plaintiff cannot use this alternative dispute resolution as a first instance. That order can only be granted by the court.²⁴³ This undermines the purpose of alternative dispute resolution. Once a plaintiff commences action in the formal courts, the matter becomes public record, they incur costs and will have to abide by the rules and procedures of civil court. The Zimbabwean Companies Act should provide a provision similar to section 166 of the South African Companies Act that allows applicants to directly pursue alternative dispute resolution without first approaching the courts.

Conclusion

The oppression remedy covers a wide range of possibilities for minority shareholders. It is also evident that the court has been granted wide discretionary powers in deciding what remedy to award. These powers must, however, be exercised in advancing the protection of minority shareholders, rather than restricting them. It must be understood that the intention of the legislature in providing a non-exhaustive relief list was in anticipation of unaccounted for events. This would allow a litigant to request an order that fits their circumstance and the legislature was correct in not limiting the relief the courts can order because this is dependent on the circumstances of each case.

²⁴⁰ *Zvandasara v Saungweme & Others* unreported judgment case no HH 108 of 2018 citing *Livanos v Swartzberg & Others* 1962 (4) SA 395 (W.L.D at 397 A-D).

²⁴¹ Zimbabwean Companies Act, section 224 (1)

²⁴² Zimbabwean Companies And Other Business Entities Act, section 61(2)(f).

²⁴³ The Zimbabwean Companies and Other Business Entities Act does not have the equivalent of section 166 of the South African Companies Act allowing for alternative dispute resolution methods. Alternative dispute resolution is only listed under the list of orders a court can grant as per an applicant's claim in a dispute.

Chapter 5: Findings on the effectiveness of minority protection in South Africa

5.1 Findings of the research

In comparison with the Zimbabwean legal system, South Africa is fairly advanced in its minority shareholder protection provisions and has made commendable advancements towards the protection of minority shareholders.²⁴⁴ For example, the derivative action was also amended to allow a wider class of persons to make use of the remedy.²⁴⁵ In another example, the list of possible relief mechanisms under sections 163 of the Companies Act is not exhaustive which allows flexibility on the part of the courts to award appropriate relief to applicants.²⁴⁶

The discussion on dissenting shareholder's appraisal rights exhibited that it is an instrument that affords minorities the opportunity to get a fair deal in the event that they have to sell their shares in certain unforeseen circumstances. It allows them to exit a company that no-longer serves their financial and business needs. Additionally, it affords them the opportunity not to be undermined by the majority shareholders. However, the uncertainty regarding the choice of a valuation method(s) that the courts will use muddies the remedy by adding. Therefore, the legislature is recommended to establish a compromise that will encourage minorities to challenge an unfair valuation. The courts in consultation with leading financial experts may come up with a list of non-exhaustive valuation methods that provide guidance to potential shareholders and the companies as to what method(s) will be employed or factors will be considered to achieve a fair result.

The derivative action places the minority shareholders in a corporate watchdog position, keeping an eye on the conduct of directors. Minority shareholders' ability to sue on behalf of the company provides a deterrent mechanism ensuring the decrease in future misconduct. Furthermore, it provides an avenue for the company to be compensated for the loss incurred at the hands of errant management. The prospect of facing public humiliation over allegations of corporate mismanagement and financial loss that could follow in the form of decreasing stock price may be an incentive to persuade the company to settle quickly and privately. However, the benefits of successfully pursuing the derivative accrues to the company but may come at a personal cost to the minority shareholders, it is thus probable that they will be hesitant to act. Although the courts have discretion in awarding costs, as mentioned above, they also have the

²⁴⁴ The oppression remedy is available to shareholders not only in terms of oppression of rights but also interests. This avails the remedy to a broader area to the advantage of minority shareholders.

²⁴⁵ Companies Act, section 165(2).

²⁴⁶ Companies Act, section 163(2).

discretion to request the shareholder to furnish the courts with security for costs. This requirement should be removed from the law because it is unjust to require persons who stand to receive no financial gain from the suit to fund it. Once a shareholder has satisfied all the requirements as provided for in section 165 of the Companies Act and stands to receive no direct benefit, the company should indemnify the shareholder, regardless of the outcome of the lawsuit.

The law ignores the reality that the parties to litigation, particularly in the context of companies and minority shareholders, may not be on equal footing. The individual minority shareholder may not have the kind of resources to match the company. Inevitably, shareholders are deterred from initiating litigation even when they have a valid claim. It is possible that companies can use this advantage to threaten minority shareholders to accept unfair offers or to drop their claim entirely. Thus, the system is structured unfavourably towards the minority shareholder and this must be rectified. Canada, for instance, does not require the security of costs from minority shareholders. Once a shareholder establishes that there is a *bona fide* case, the court is obliged to indemnify them against costs. The company must bear such costs. A system of that nature will serve to deter any impropriety within companies for fear of heavy legal costs burdens. It is recommended for the legislature to consider amending the law to ease the burden of the minority shareholders.

What emerges in every remedy discussed in this paper is that the Companies Act places a heavy burden of proof and procedural requirements²⁴⁷ on the minority shareholder seeking relief. There are procedural formalities with penalties for not adhering to such formalities. This can be understood as a necessary measure to guard against the broadness of the remedies. Without such limitations, the courts may be flooded with frivolous and ambiguous claims. It is therefore important to provide a balance that whilst the procedural requirements guard against abuse of the law they also do not deter its utilisation.

There are other factors exclusive to amending the three shareholder remedies that can be useful in ensuring the effectiveness and practicality of minority shareholder protection remedies. These factors are discussed below.

²⁴⁷ The strict procedural requirements under Companies Act, section 164 and the burden to satisfy the three-pronged test for an application for leave to sue on behalf of the company under section 165 of the same Act can become burdensome for a shareholder and become a deterrent.

5.2.1 Considerations of a Specialised Commercial Court

Throughout the discussion and analysis of the procedures involved with the three remedies, the thesis alluded to the problems associated with litigation. Litigation is an adversarial process that is loaded with strict procedural requirements. The process of litigation is generally lengthy, and attempts must be made to redirect the focus of companies from the courts back to the board room. Whilst alternative dispute resolution is one choice, there could also be another. The Gauteng province gazetted a circular for the reintroduction of a special commercial court.²⁴⁸ This court will be dedicated to specific commercial matters. Streamlining the matters that can be adjudicated by the courts will result in a smaller caseload for the courts resulting in the courts having more time to go through smaller caseloads. As a result, the commercial court will be able to hear and dispose of matters at a quicker rate than an ordinary court burdened with other matters.

The special court aims to promote the conduct of litigation and facilitate dispute resolution in a quick, cheap fair manner with legal acuity.²⁴⁹ However, the specialised court is not completely divorced from the ordinary court process. Litigants will have to in the first instance approach the High Court, then seek a referral to the commercial court²⁵⁰ upon satisfying certain criteria. Litigants are required to submit a written request to the Judge President justifying the need for the matter's referral to the commercial court.²⁵¹ The opposing party is allowed to make representations in support or against the referral of the matter. Although on the face of it the idea of the commercial court is appealing, the process of obtaining the referral itself could turn into a mini-trial. In the end, this can prolong the litigation process from the ordinary court to the commercial court. The selection of the Judges is handled by the Judge President or Deputy President.²⁵² However, the court does not stipulate any peculiar qualifications for Judges to qualify for appointment to the commercial court. It is recommended that only judges with expertise in handling commercial matters must be appointed to the commercial court. It is anticipated that their knowledge and expertise will instil confidence in the litigants themselves thus dispensing with the need for expert witnesses. This may in turn reduce the cost of litigation. What will a specialised court do, reduce time, procedure still there, costs still there, formality still there, therefore not much difference, serve in time and

²⁴⁸ Commercial Court Practice Directive of 2018 Chapter Chapter1:1.

²⁴⁹ Commercial Court Practice Directive, Chapter 1:1.

²⁵⁰ Commercial Court Practice Directive, Chapter 2:1.

²⁵¹ Commercial Court Practice Directive, Chapter 2:2.

²⁵² Commercial Court Practice Directive, Chapter 2:7.

Concluding remarks

This thesis set out to enquire whether three specific minority shareholder provisions were effective and practical in affording minorities' protection of their rights. What is clear is that South Africa has, for the most part, made commendable strides towards availing the remedies to a wider group of persons and enlarging the scope of the area that the remedies apply to than before. This is particularly true of the oppression remedy which despite only being available to directors and shareholders has been extended to allow the said persons to not just sue for the oppression of their rights but also interests. Appraisal rights are a welcome relief affording minorities the option to exit a company, albeit in limited circumstances with the assurance of a buyer who is mandated to pay a fair price for the share. The derivative action has been made available to a wider class of persons and the courts have been granted the ability to decide persons who in their view are legible to bring an action.

There was comparison with the Zimbabwean legal system and this process highlighted that Zimbabwe has much room to improve towards the betterment of minority shareholders. What could be observed in both systems are there is a heavy procedural burden on the minority shareholders. Whilst the substance of the provisions themselves is sound, the ancillary requirements may make the remedies unattainable for most individual shareholders. In conclusion, there is always room for the development of the law. The legislature must continuously seek to make the law clear and reasonably accessible to those it is intended to help. The conclusion lies in that minority shareholders provisions in the law provide a window of opportunity for the protection of minority shareholders. However, there are several factors diminishing the effectiveness and practicality of the said measures. The law can be altered to eliminate the grey areas surrounding the calculation of fair value for appraisal right. The law could be amended to indemnify bona fide shareholders against the cost of suit in a derivative action or oppressive remedy. Finally, the law can be easily amended to insert provisions clearly stating the availability of alternative dispute resolution for company disputes of any nature. Until such a time as and when these areas are attended to the protection of minority shareholders remains imperfect.

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